# HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** HB 251, 1ST ENG. Firefighter and Municipal Police Pensions
**SPONSOR(S):** Sansom, and others
**TIED BILLS:** none **IDEN./SIM. BILLS:** CS/SB 654

| REFERENCE | ACTION | ANALYST | STAFF DIRECTOR |
|---|---|---|---|
| 1) State Administration | | Bond | Everhart |
| 2) | | | |
| 3) | | | |
| 4) | | | |
| 5) | | | |

## SUMMARY ANALYSIS


Current law encourages municipalities and special fire districts to create firefighters' and police officers' pension plans by permitting such municipalities and special districts to enact a premium tax on property insurance policies insuring property in their jurisdiction provided such plans meet certain requirements. Most municipalities and special fire districts participate in the plan. The insurance companies who collect the tax are also responsible for indicating where the property lies (its "situs") in order that the proper municipality or special district receives its proper share of the premium tax. The municipalities and special districts believe that a significant amount of the tax is not properly collected and paid over due to situs errors by insurance companies. This bill requires the Department of Revenue to create an electronic database that insurance companies can use to determine the situs of property and casualty insurance policies. Through 2007, municipalities with police retirement plans under chapter 185, F.S., are guaranteed at least as much revenue from the tax on casualty insurance premiums as they received in 2004, unless overall premium tax collections decrease.

The Division of Retirement has interpreted current law to require that a municipality or special district may only use the increases in premium tax revenues received after 1997 to fund new employee benefits enacted after March 12, 1999. Municipalities have disputed this interpretation, their appeal of an adverse administrative ruling is currently pending before the First District. This bill adopts the interpretation of the Division of Retirement that "extra benefits" means those benefits in addition to those in existence for firefighters or police officers on March 12, 1999.

This bill also provides for deductions from retirement pay due to a retiree for benefits, union dues, and other payments required by law. There is a concern that, as written, these provisions may have the unintended consequence of allowing garnishment or alienation of a retiree's retirement account. See "Drafting Comments or Other Issues" herein.

This bill provides a nonrecurring $300,000 appropriation, and a recurring appropriation from trust funds of $100,000, adjusted annually for inflation. This bill has a significant but indeterminate recurring fiscal impact on local governments. There are technical concerns regarding the appropriations, see "Fiscal Comments" herein.

## FULL ANALYSIS

## I. SUBSTANTIVE ANALYSIS

A. DOES THE BILL:

| | | | |
|---|---|---|---|
| 1. Reduce government? | Yes[] | No[x] | N/A[] |
| 2. Lower taxes? | Yes[] | No[x] | N/A[] |
| 3. Expand individual freedom? | Yes[] | No[] | N/A[x] |
| 4. Increase personal responsibility? | Yes[] | No[] | N/A[x] |
| 5. Empower families? | Yes[] | No[] | N/A[x] |

For any principle that received a "no" above, please explain:

The Department of Revenue (DOR) is directed to create an electronic database, maintain the database based on information that municipalities and special districts must provide, audit insurance agencies, and assess fines against noncompliant insurance companies.

B. EFFECT OF PROPOSED CHANGES:

**Background**

Municipal and Special District Firefighters' and Police Officers' Pension Plans - In General

Chapters 175 and 185, F.S., regulate and provide funding for municipal and special district firefighters' and police officers' pension plans. Chapter 175, F.S., regarding firefighter pensions, was originally enacted in 1939. Special fire control districts became eligible to participate under ch. 175, F.S., in 1993. In 1953, very similar ch. 185, F.S., was created for police pensions. Both chapters set up a uniform retirement system providing defined-benefit retirement plans for firefighters or police officers, setting standards for operation and funding of these pension systems. Municipalities and special districts that elect to create plans governed by these chapters may impose a premium tax[1] on property insurance covering properties within their jurisdiction. Statewide, 175 municipalities and special districts have pension plans for firefighters subject to ch. 175, F.S., and 184 cities have pension plans for police subject to ch. 185, F.S. The premium tax generated approximately $94 million in 2002.

Retirement plan funding comes from the premium tax, employee contributions, and other pledged revenue sources. If these sources are insufficient, the municipality or special district must pay what is necessary to keep the plan actuarially sound. Responsibility for overseeing and monitoring these plans lies with the Division of Retirement of the Department of Management Services, but day-to-day operational control rests with local boards of trustees.

When a property insurance policy is written, the insurance agent is supposed to report to the insurance company whether the property is located within a district making the policy subject to a premium tax. The insurance company is then liable for collecting the tax, reporting aggregate monies to each district, and paying the tax collected over to the state. The Department of Revenue collects the tax, and reports the aggregate collections from all insurance companies to the Division of Retirement, which distributes the appropriate funds to each district. Insurance companies are subject to examination by the Office of Insurance Regulation pursuant to ss. 624.316 and 624.3161, F.S., and may be disciplined for failure to properly manage the assignment of properties to districts and the collection of taxes thereon.

In practice, the current system has several flaws. There is no uniform method for agents to use in initial determination of whether a property lies within a municipality or special fire district, nor for use in assignment of a property to the correct municipality or special fire district. There is no method by which

[1] The rate under ch. 175, F.S., is 1.85% of the premium; the rate under ch. 185, F.S., is 0.85%.

insurance companies can recognize annexations that would make a renewal policy subject to the premium tax. There is little enforcement of sanctions against insurance companies who are negligent in their reporting; and thus little incentive for insurance companies to provide accurate reporting. Municipalities and special fire districts believe that the combined effect of these flaws is that millions of dollars in premium tax revenue is not collected, or if collected is paid to the incorrect district.

Additional Premium Tax Revenues used for "Extra Benefits"

Sections 175.351 and 185.35, F.S., provide minimum standards for pension plans to qualify for distributions of insurance premium tax revenue under s. 175.101 and 185.08, F.S. In 1999, the Legislature substantially revised the laws governing retirement plans for firefighters and police officers. One change provides that premium tax revenues exceeding the amount received in 1997 may only be used by a municipality to fund "extra benefits" provided to firefighters and police officers, that is, retirement benefits greater than those provided to the general employees of the municipality.

In 2003, the Division of Retirement adopted a rule that provides that municipalities cannot use premium tax revenues to fund extra benefits unless the extra benefits were adopted after March 12, 1999, the effective date of the 1999 revisions. Therefore, municipalities that granted their firefighters and police officers extra benefits prior to March 12, 1999, must use other revenues to fund these extra benefits, rather than continue to use premium tax revenues.

Municipalities argue that there is no legal authority for the Division's interpretation and rule. The rule has, however, been upheld by a hearing officer.[2] The municipalities have appealed the administrative ruling to the First District.

**Effect of Bill**

The Local Taxing Jurisdiction Data Base

This bill requires the Department of Revenue, subject to legislative appropriation, to create and maintain a database for use by insurance agents and companies in determining the situs of a insured parcel. The database is to follow the American National Standards Institute's Accredited Committee X12, and is to designate for each street address and address range in the state the local taxing jurisdiction in which the address is located and the code for each local taxing jurisdiction. This database is to be updated annually based on annexation information that municipalities and special districts will be required to provide to DOR.[3]

An insurance company that exercises due diligence[4] in employing the database will be held harmless from any liability related to payment of the tax. Additionally, insurers are held harmless from any liability related to payment of the tax prior to January 1, 2006, if the insurer reports taxes prior to that date consistent with filings for previous periods. An insurance company that does not utilize due diligence in reporting may be subject to a penalty of 0.5% of the tax paid.[5]

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[2] *Florida League of Cities v. Dept. of Management Services*, Case No. 03-1117RP, Final Order dated September 23, 2003.

[3] Each participating local taxing jurisdiction must provide DOR all the information needed to create and update the original database and each annual database. The information for an update must be provided to DOR by July 1 of each year. The department is required to post each new annual database on the Internet by September 1 of each year, if possible, and allow the municipalities and fire control districts 30 days in which to review the database and provide corrections. Also, DOR is required to finalize the annual database and posit it on a website by November 1.

[4] Due diligence is defined to include: assigning policies based on the department's database; expending reasonable resources to accurately and reliably implement the use of the database; maintaining adequate internal controls to correctly include the location of the insured property in the proper address format; and, correcting errors in the assignment of addresses to local taxing jurisdictions within 120 days of discovering the error.

[5] It is unclear whether this penalty is sufficient to deter insurance companies from continuing to file inaccurate returns of the premium tax. If every insurance company in the state were to be found to not be acting with due diligence, the penalty

As to the premium tax distribution under s. 185.08, F.S. (police officers), distributions to a municipality for calendar years 2005-2007 may not be reduced below the 2004 distribution to that municipality unless total premium tax collections decrease.[6]

Additional Premium Tax Revenues used for "Extra Benefits"

This bill adopts the interpretation of "extra benefits" adopted by the Division of Retirement.

Non-recurring and Recurring Appropriation

The bill appropriates $300,000 upon enactment to the Department of Revenue for use in creating the database. The bill also authorizes recurring appropriations payable to DOR from the Police and Firefighter's Premium Tax Trust Fund for the annual maintenance cost; limited to $100,000 in the first year, which limit is increased by an inflationary adjustment in future years. There are technical concerns regarding the form of the appropriations, see Fiscal Comments herein.

Deductions from Retirement Pay

This bill provides that police and firefighter pensions plans may deduct from any payment due to a retiree any amount authorized by the retiree for benefits, for union dues, or for court-ordered payments (which may include assignments, garnishments, judgments, or even taking by a bankruptcy court).

C. SECTION DIRECTORY:

Section 1 creates s. 175.1015, F.S., relating to firefighter pensions, to create the database, and require insurance companies to use.

Section 2 creates s. 185.085, F.S., relating to municipal police pensions, to create the database and require insurance companies to use it. Additionally, this section prohibits a decrease in the allocation to a municipality for three years.

Sections 3 and 4 adopt the Division of Retirement interpretation of "extra benefits."

Sections 5 and 6 provide that retirees may authorize deductions from their retirement pay for benefits (such as health and life insurance), union dues, and other payments required by law.

Section 7 provides a nonrecurring appropriation of $300,000 from the General Revenue Fund.

Section 8 provides legislative findings necessary should this bill be found to be a mandate.

Section 9 provides an effective date of upon becoming law.

## II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

   Minimal. An insurance company that fails to use the database or due diligence in the collection and remittance of the tax may be penalized. The anticipated amount of such penalties, if any, is

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would only be $465,000. If the cost of compliance exceeds the potential penalty, it is possible that insurance companies may make the economic choice of simply paying the penalty.

[6] In the unlikely event that premium tax revenues were to decrease statewide, a prorata distribution formula is provided.

unknown. If every insurance company was penalized, the total (based on 2002 collections) would be $465,000. Sections 175.121(1), and 185.10, F.S., provide that all monies collected under chapters 175 and 185, F.S., are to be deposited in the Police and Firefighters' Premium Tax Trust Fund.

2. Expenditures:

This bill requires a $300,000 nonrecurring appropriation from the General Revenue Fund to DOR for initial creation of the database. The bill further requires an annual appropriation from the Police and Firefighter's Premium Tax Trust Fund to cover annual maintenance costs, which is limited to $100,000 in the first year and is increased thereafter by an inflationary adjustment.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

Unknown. It is possible that more accurate reporting will result in the collection of the tax regarding properties that are currently not being assed the tax. This amount is unknown.

2. Expenditures:

Creation and Maintenance of the Database Issue: Municipalities and special districts are required by this bill to provide the initial information necessary to creation of the database, and will be required to provide change information in future years. They have not provided any estimate of their expected cost to comply with this requirement.

Extra Benefits Issue: If the position of the Division of Retirement, which has been upheld in an administrative ruling, is upheld on appeal before the First District, then this bill does not represent a fiscal cost to municipalities. The Florida League of Cities argues that, if their position is correct, this bill represents a recurring negative fiscal impact of $2 million to municipalities.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Private sector insurance companies may be impacted by two provisions of this bill. First, this bill penalizes insurers (0.5% penalty) who fail to properly collect and account for the premium tax. Second, it is unclear whether this bill will increase or decrease the administrative and reporting burden on insurance companies for compliance with the premium tax law. Insurance companies have not provided any estimate of whether they will realize additional savings, or incur additional costs, as a result of this bill.

D. FISCAL COMMENTS:

Because the effective date is "upon becoming law", it is unclear whether the $300,000 nonrecurring appropriation is payable in FY 2003-2004 or FY 2004-2005. If paid in FY 2003-2004, the disbursement cannot be from the General Revenue Fund. Because the effective date is "upon becoming law", it is unclear whether the $100,000 recurring appropriation will commence in FY 2003-2004 or FY 2004-2005. It is unclear why the recurring appropriation for maintenance would be required during the creation and implementation phase. The Department of Revenue has stated that they would only require $50,000 annually for maintenance of the database, not $100,000.

It is unclear which agency or division (the Department of Revenue, the Office of Insurance Regulation, or the Division of Retirement) is responsible for auditing insurance companies, is responsible for determining whether insurance companies have exercised due diligence in collection and reporting of the tax, or is responsible for enforcement of the penalty. Because any collected penalty would be paid to the trust fund and distributed to participating municipalities and special fire districts, it is unclear how, or if, the regulatory function is funded.

## III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

This bill requires all municipalities, whether or not they participate in the retirement programs, to provide initial and ongoing boundary and annexation information necessary to creation of the database. The cost of compliance with this requirement is likely to be far below the definition of an "insignificant fiscal impact." See art. VII, s. 18(d), Fla.Const.

The provision in this bill regarding "extra benefits" may require municipalities to expend additional funds only if the Division of Retirement's interpretation of the 1999 amendments regarding extra benefits, adopted by this bill, is not the correct interpretation of previous changes to chapters 175 and 185, F.S.[7] This bill contains a finding that it fulfils an important state interest.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

The bill requires that DOR adopt rules necessary to administer the new statutes; these rules must include procedures and forms.

C. DRAFTING ISSUES OR OTHER COMMENTS:

The provisions in sections 5 and 6 that allow for deductions from retirement pay for any "payment required by law" may perhaps make such plans subject to creditor claims (including attachment, garnishment, and seizure by a bankruptcy court), and thus may be in conflict with the protections of s. 175.241, F.S., and s. 185.25, F.S.

## IV. AMENDMENTS/COMMITTEE SUBSTITUTE CHANGES

On March 3, 2004, the House adopted one amendment that:

- Broadens the immunity for insurance companies from "liability for taxes, interest or penalties" to "any liability", and extends the immunity for one year to January 1, 2006.
- Defines due diligence as it relates to commercial policies.
- Corrects incorrect references to 2002 to 2004.
- Removes the requirement that the Department of Revenue furnish a free copy of the database to any property insurance company.
- Adds a statement that the changes of this bill fulfill an important state interest.

The bill was then referred to the Committee on State Administration.

[7] That interpretation was upheld by the Division of Administrative Hearings, and is currently on appeal to the First District.